FEDERAL COURT OF AUSTRALIA

Progressive Direct Insurance Company, application under the *Insurance Act 1973* (Cth) (No 2)[2018] FCA 9

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| File number: |  |
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| Judge: | **FARRELL J** |
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| Date of judgment: | 15 January 2018 |
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| Catchwords: | **INSURANCE** – application to approve scheme for transfer of insurance business – transfer from Australian branch of foreign company to Australian company – whether scheme in best interests of policyholders – application granted |
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| Legislation: | *Corporations Act 2001* (Cth)  *Insurance Act 1973* (Cth) ss 17C, 17F |
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| Cases cited: | *Progressive Direct Insurance Company, application under the Insurance Act 1973* (Cth) [2017] FCA 1106  *Re Munich Reinsurance America Inc, in the matter of Munich Reinsurance America Inc (No 2)* [2011] FCA 9  *Re Westport Insurance Corporation (No 2)* (2009) 181 FCR 530; FCA 1598 |
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| Date of hearing: | 10 November 2017 |
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| Registry: |  |
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| Division: |  |
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| National Practice Area: | Commercial and Corporations |
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| Sub-area: | Commercial Contracts, Banking, Finance and Insurance |
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| Category: | Catchwords |
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| Number of paragraphs: | 28 |
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| Counsel for the Applicant: | Mr M A Izzo |
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| Solicitor for the Applicant: | Clayton Utz |
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| Counsel for the Hollard Insurance Company Pty Ltd: | Mr M F Newton |
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| Solicitor for the Australian Prudential Regulation Authority: | Ms S Neumueller of Australian Prudential Regulation Authority |

ORDERS

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|  | | NSD 1452 of 2017 |
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| APPLICATION OF PROGRESSIVE DIRECT INSURANCE COMPANY UNDER THE *INSURANCE ACT 1973* (CTH) | | |
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|  | PROGRESSIVE DIRECT INSURANCE COMPANY (ABRN 140 389 528) | |
|  | Applicant | |

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| JUDGE: | Farrell J |
| DATE OF ORDER: | 10 NOvember 2017 |

THE COURT ORDERS THAT:

1. Pursuant to section 17F of the *Insurance Act 1973* (Cth), the scheme for the transfer of the business of the Australian branch of the applicant to The Hollard Insurance Company Pty Ltd, as set out in Exhibit B is confirmed subject to the following modification: the definition of **Effective Time** is amended to read: “Effective Time means 12 am Australian Eastern Daylight Time on 11 November 2017”.
2. The applicant to pay the costs of the proceeding of APRA to date, as agreed on or assessed.
3. This order be entered forthwith.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

REASONS FOR JUDGMENT

FARRELL J:

1. On 10 November 2017 the Court made an order under s 17F(1) of the *Insurance Act 1973* (Cth) (the **Act**) confirming a **scheme** toeffect the transfer of all rights and obligations under all contracts of motor vehicle insurance (including expired contracts) that Progressive Direct Insurance Company (**PDIC**) has issued, renewed, underwritten or assumed through its Australian branch and its Business Assets (as defined in the scheme) to The Hollard Insurance Company Pty Ltd (**Hollard**) and ancillary orders. These are my reasons for making those orders.
2. On 18 September 2017, orders were made dispensing with the need for compliance with s 17C(2)(c) of the Act subject to conditions (**dispensation orders**): see *Progressive Direct Insurance Company, application under the Insurance Act 1973* (Cth) [2017] FCA 1106.

## Submissions and evidence

1. PDIC filed written submissions dated 2 November 2017 which were marked for identification as MFI-1 (**November submissions**). Submissions filed in support of the application for the dispensation orders were marked as MFI-2.
2. The application was supported by the affidavits listed in paragraph 2 of the November submissions. Some of the dates of the affidavits as listed changed due to errors which required the affidavits to be re-executed without change to their substance. Two further affidavits were filed on 9 November 2017 and a further affidavit was tendered at the hearing, being an affidavit affirmed by Brian James Thomas on 8 November 2017, an affidavit affirmed by Lucy Louise Terracall on 9 November 2017 and an affidavit sworn by Roland Covac Lange on 10 November 2017. It was also supported by a letter dated 7 November 2017 from PC Soebrati and JA van Voorst Vader, Managing Directors of Hollard Investments BV (**HIBV**) (**investment intention letter**), in relation to the provision of $40 million to Hollard as “tier 2” capital (**capital injection**).
3. The Court relied on the written submissions and submissions made at the hearing on 10 November 2017 by counsel for PDIC, Mr Izzo, counsel for Hollard, Mr Newton and solicitor for the Australian Prudential Regulatory Authority (**APRA**), Ms Neumueller and the supporting affidavits in relation to the matters set out below.

## Brief background

1. At the time the application to confirm the scheme was heard:
2. PDIC was a registered foreign company under the *Corporations Act 2001* (Cth) and it was authorised to carry on insurance business in Australia. The motor vehicle insurance business was the only business which PDIC conducted in Australia. Relevant features of this business are referred to in the section of these reasons dealing with the actuary’s report.
3. PDIC was an indirect wholly owned subsidiary of The **Progressive** Corporation, a public company listed on the New York stock exchange, with consolidated assets of US$36.7 billion, total liabilities and redeemable non-controlling interest of US$27.7 billion and shareholders’ equity of US$9 billion as at 30 June 2017. Progressive’s public debt has been rated “A” by AM Best, “A” by Fitch, “A2” by Moody’s and “A” by S&P. Although Progressive is not itself an insurance company, its insurance subsidiaries and affiliates (including PDIC) have ratings of “A+” from AM Best, “AA” from Fitch, “Aa2” from Moody’s and “AA” from S&P.
4. PDIC wished to exit the Australian market and its preference was to do so by transferring its portfolio to Hollard so that policyholders would have continuity with their motor vehicle insurance and no further need to deal with PDIC after the Effective Time. If this could not be done, PDIC’s business in Australia would go into run-off, with no new policies being issued. PDIC advised the Court that, if the scheme was confirmed, it would apply to APRAto have its authorisation to carry on insurance business in Australia revoked.
5. To facilitate the implementation of the proposed scheme and PDIC’s exit from the Australian market, in March 2017, PDIC, Hollard, PD Insurance Agency Pty Ltd (**PDIA**) and various other parties entered into an Implementation Deed which contemplated a number of transactions. Those transactions included the appointment of PDIA as PDIC’s agent and authorised representative in Australia to issue, renew and administer motor vehicle policies issued by PDIC before transfer under the scheme and for Hollard after transfer. Hollard also entered into an agency agreement with PDIA pursuant to which PDIA will market, issue and administer Hollard’s motor vehicle insurance policies with the result that, after the scheme is implemented, PDIA will continue to manage claims, albeit under a new claims structure. Simon Greger Lindsay, who was involved in the establishment of PDIC’s business in Australia, was appointed as Managing Director of PDIA and he will continue to manage the portfolio as an employee of PDIA following implementation of the scheme.
6. With effect form 31 March 2017, new claims from PDIC’s Australian branch were reinsured by Hollard (with a 100% quota share) under a reinsurance treaty it entered into with PDIC on 8 March 2017. Hollard had reinsured this liability with a panel of external reinsurers and it retains a net 65% exposure to claims made after 31 March 2017; this reinsurance treaty would extend to policies transferred to Hollard upon implementation of the scheme. Hollard also has large loss catastrophe reinsurance which will cover its liability under its reinsurance treaty with PDIC and policies transferred to it upon implementation of the scheme.
7. Hollard was incorporated in New South Wales and authorised to carry on an insurance business in Australia. It was a multi-line insurer underwriting several types of insurance for commercial entities and individuals, with gross premiums of $718 million in the financial year ended 30 June 2017. The majority of its business was personal lines and its book included vehicle insurance policies.
8. Hollard’s immediate parent was HIBV, a company incorporated in the Netherlands and ultimately owned by **IVM Intersurer** B.V. As at 30 June 2017, HIBV’s total assets were $620,334,970, total liabilities were $299,792 and shareholder equity was $620,035,178. The only insurance policy liabilities and premium revenues of HIBV group entities were those of Hollard. Both IVM Intersurer and HIBV were non-operating holding companies. Hollard had a financial strength rating of “A-” (excellent) from AM Best, the second highest of seven categories.
9. HIBV was Hollard’s principal source of capital funding. Since 30 June 2017, HIBV received repayment of a $300,000,000 loan it had made to IVM Intersurer. Those funds were deposited into bank accounts in HIBV’s name. On 30 August 2017, HIBV advised Hollard that there was A$40 million available in cash for immediate investment and of its intention to invest those funds once an appropriate “tier 2” instrument had been approved by APRA. It stated its intention to make the investment as soon as possible and no later than 31 December 2017. However, on around 1 November 2017, APRA advised that it would take eight weeks for requisite approvals to be obtained, making it unlikely that the investment could occur by the end of calendar year 2017 as no draft instrument had been submitted to APRA at that time. By the investment intention letter tendered at the hearing, HIBV confirmed that if finalisation of APRA’s approval extended beyond 31 December 2017, it would make the capital injection as soon as possible after the approval was obtained.
10. Tim Andrews, an actuary employed by Finity (**actuary**), had issued a report dated 8 June 2017 in relation to the impact of the scheme on the interests of policyholders of PDIC’s Australian branch (referred to as **PDIC Aus**) and Hollard (**Finity Report**), an updating letter dated 15 September 2017 (**Supplementary Report**) and a further updating letter dated 31 October 2017 (**Second Supplementary Report**). The Second Supplementary Report superseded the Supplementary Report. At page 11 of the Second Supplementary Report, the actuary said (as written, emphasis added):

**Opinion**

Having undertaken the additional analysis set out in this letter, my opinion is unchanged: namely that the interests of the policyholders of PIDC Aus and Hollard will not be adversely affected in a material way as a consequence of the Insurance Scheme.

This opinion is based on the planned capital injection taking place by December 2017. The reasons that I have for considering that the injection is likely are set out in Section 3. **If the injection were not made, then my opinion could change**.

1. APRA did not object to the proposed scheme or to the orders sought by PDIC being made.

## Section 17F of the Act and relevant principles

1. Section 17F of the Act is the source of the Court’s authority to confirm a scheme. It provides as follows:

**17F Confirmation of scheme**

1. The Federal Court may:

(a) confirm a scheme without modification; or

(b) confirm the scheme subject to such modifications as it thinks appropriate; or

(c) refuse to confirm the scheme.

(1A) In deciding whether to confirm a scheme (with or without modifications), the Federal Court must have regard to:

(a) the interests of the policyholders of a body corporate affected by the scheme; and

(b) if a report relevant to all or part of the scheme has been filed with the Court under s 62ZI – that report; and

(c) any other matter the Court considers relevant.

(2) The Federal Court may make such orders as it thinks fit in relation to reinsurance.

1. A critical factor on an application of this kind is whether implementation of the scheme will materially detrimentally affect policyholders of both PDIC and Hollard. Although an “affected policyholder” is defined in s 17C of the Act as referring to the holder of a policy being transferred, the effect the scheme will have on other policyholders of both the transferor and transferee companies is not irrelevant. However, where a company is foreign (as PDIC is) only the interests of policyholders of the Australian branch need be taken into account: see *Re Westport Insurance Corporation (No 2)* (2009) 181 FCR 530; FCA 1598 per Lindgren J at [32]-[33] and [49] and *Re Munich Reinsurance America Inc, in the matter of Munich Reinsurance America Inc (No 2)* [2011] FCA 9 per Stone J at [11]-[13].

## Issues of particular focus

1. Issues of particular focus were:
2. There was no opposition to the scheme being confirmed. The adequacy of notice to policyholders was in issue having regard to the change of the date of the hearing of the application to confirm the scheme from 3 November 2017 to 10 November 2017 and the change of location of the hearing to the premises of the Family Court of Australia in the Lionel Bowen Building at Goulburn Street, Sydney due to the temporary closure of the Law Courts Building at Queens Square in Sydney.
3. Compliance with formal requirements, including the dispensation orders.
4. The Effective Time, defined as 4 November 2017 in the scheme as notified to the public and provided in advance to APRA, was a date earlier than the hearing.
5. The timing of the proposed $40 million “tier 2” capital injection by HIBV.
6. Migration of policy information and claims management to a new platform.

### No opposition to the scheme – adequacy of notice

1. No policyholder appeared to oppose the scheme and no notice was received of any policyholder’s intention to do so. Although both the date and location of the hearing of the application to confirm the scheme changed, the Court was satisfied that any policyholder who wished to be heard was in a position to do so.
2. Daniel Mark Trudgen, the director of management reporting and planning for PDIC, Brian James Thomas, a solicitor principal of MacKenzie Thomas Lawyers, solicitors for Hollard and Richard James Heilig, Hollard’s chief operating officer, gave evidence on the basis of which the Court understood that links from PDIC’s website (progressiveonline.com.au) and Hollard’s website (www.hollard.com.au) each contained links to the website (progressivehollardscheme.com) (**scheme website**). From 3 October 2017, the scheme website displayed copies of the scheme summary, notice of intention, the scheme, the Finity Report and Supplementary Report. From about 26 October 2017, it contained a notification as follows:

UPDATE: The Application to the Federal Court of Australia in Sydney is now to be made on 10th of November 2017 at 10.30 am and the Scheme Call Centre will be open until 10th of November 2017.

1. The primary method of communication with policyholders was via PDIC’s website. Further, a hotline had been established and it was in operation throughout the period to 10 November 2017.
2. Ms Lucy Louise Terracall, a partner at Clayton Utz, gave evidence that:

* No notice of intention to appear was received, based on completed summaries of incoming calls to the enquiries hotline in relation to the scheme and the advice of the “contact persons” set out in the notice of intention; and
* On 3 November 2017, a lawyer employed by Clayton Utz attended at the Registry of the Federal Court (which had been removed to the ground floor of the premises of the Family Court of Australia at the Lionel Bowen Building, 97-99 Goulburn Street, Sydney due to the temporary closure of the Law Courts Building at Queens Square) and no one appeared.

### Compliance with formal requirements and dispensation orders

1. The affidavits read relate to the steps taken to comply with the dispensation orders and to satisfy the formal requirements imposed by the Act; they are summarised at [44]-[63] of the November submissions. The Court was satisfied that they adequately address those issues.
2. For completeness, counsel for PDIC drew to the Court’s attention the fact that the notice of intention was published in the required publications on 4 October 2017, while the notice of intention stated that the relevant documents would be available for inspection “for a period of at least 15 days from 3 October 2017” and those documents were in fact at the locations specified in the notice of intention from that date. The Court was satisfied that items 11, 16 and 17 of the *Prudential Standard GPS 410* were satisfied in this case having regard to the evidence that:

* The scheme document was not released to any member of the public at the specified locations before 4 October 2017 (or at all, since no member of the public requested inspection of the documents); and
* More than 15 business days elapsed following publication of the notice of intention during which a member of the public could have obtained access to the scheme document (and the other relevant documents) from the specified locations and before the hearing of the application for confirmation of the scheme. The last date on which the relevant documents were available at the specified locations was 8 November 2017.

### Effective Time

1. Section 17F(1)(b) permits the Court to confirm a scheme subject to modifications. In this case, it was necessary to modify the “Effective Time” so that all rights and obligations under all contracts of PDIC’s motor vehicle insurance policies may be transferred to Hollard. Without the modification, policies entered into after 4 November 2017 but before the scheme was confirmed would not be transferred as part of the scheme. Accordingly, the Court determined that confirmation of the scheme should be made subject to this modification.

### Actuarial reports and HIBV tier 2 capital injection

1. The actuary’s opinion as set out in the Finity Report was that the interests of policyholders of PDIC’s Australian branch and Hollard would not be adversely affected in a material way as a consequence of the implementation of the scheme. In reaching this conclusion, the actuary considered the nature of the business to be transferred, policy terms and premium rates, claims handling, risk profile and financial security.
2. At section 2.1 of the Finity Report, the actuary said (as written):

**2.1 Nature of the Business to be Transferred**

The PDIC Aus portfolio represents around 30 million of domestic motor business. The portfolio is small in the context of the Hollard business, representing around 5% of Hollard premium levels.

Domestic motor business tends to be ‘short tailed’, which means that claims are paid out relatively quickly after they occur. This is relevant in the context of the scheme as it means that there are low levels of uncertainty attaching to the claims liabilities.

From 31 March 2017 the PDIC Aus portfolio has been 100% reinsured by Hollard for all premiums earned from that date. The extra risk being transferred to Hollard as a result of the scheme relates to claims that occurred prior to 31 March 2017 but which still remain to be paid on the scheme date. Given that more than eight months will have elapsed by the time of the scheme, unpaid claims and hence the extra risk being transferred to Hollard as a result of the scheme is expected to be small.

1. At section 2.2 of the Finity Report, the actuary said (as written):

**2.2 Policy Terms and Premium Rates**

There will be no changes to the terms and conditions of current and prior policies issued by PDIC Aus as a result of the scheme.

In the event that Hollard changes the terms and conditions for new contracts in future, this will not impact current PDIC Aus policyholders for the remaining term of their contracts. Similarly, while premium rates for some policyholders will change for future periods of insurance, such changes are part of normal insurer operations.

In this context, PDIC Aus’s policyholders will be in the same position as before the scheme.

1. At section 2.3 of the Finity Report, the actuary noted that claims would be managed by the same team before and after implementation of the scheme so that management philosophy and guidelines will initially broadly be unchanged and that while changes may subsequently occur, that would be possible whether or not the scheme was implemented. On that basis, there was no reason to believe that policyholder and claimant expectations in relation to claims handling would be materially affected by the scheme.
2. In relation to the financial security of PDIC’s Australian branch policyholders, the actuary said at section 2.5.1 of the Finity Report (as written):

**2.5.1 PDIC Aus Policyholders**

PDIC Aus has been making substantial underwriting losses. As such the protection provided to the policyholders has been dependent on the branch holding additional capital in Australia to reflect the level of projected losses as well as regular injections of capital from the parent. The parent is a large well rated (S&P AA) US company with a book value of US$8 billion. The potential level of protection provided to policyholders is thus substantial currently.

On transfer to Hollard the policyholders will be subject to a wider range of risks than they were previously, reflecting the more complex nature of the Hollard business. However, in my opinion the financial security for the PDIC Aus policyholders will not be adversely affected to a material extent post-scheme for the following reasons:

* Firstly, as a result of the short tailed nature of the business, the period for which the transferring policyholders are exposed to any extra risk is short, noting they have the option at renewal to transfer to other insurers.
* Post-scheme, Hollard’s capital adequacy multiple is estimated to be 1.63 times APRA’s minimum requirements. This represents a substantial level of capital in its own right. The capital level will be within Hollard’s normal operating range. The Hollard operating range for capital is higher than the equivalent figures for PDIC Aus.
* Certain of Hollard’s assets which are inadmissible for APRA purposes can be seen as having some value - i.e.in effect a capital adequacy is better than the capital adequacy multiple of 1.63 shows.
* In Australia the Hollard portfolio is larger, more profitable and more diversified than the PDIC Aus business. This reduces the likelihood of capital being needed to support payments to policyholders.
* Like PDIC Aus currently, Hollard is supported by a parent company. Furthermore Hollard’s dependence on the parent is lower than PDIC Aus’s, noting the better profitability of Hollard. While the Hollard shareholders may ultimately not have the same financial resources as PDIC US, I note that they have demonstrated a preparedness to make capital injections into the business we needed in the past.
* Hollard has significant reinsurance protection which limits the volatility of performance and is used by the company to provide capital relief. In addition this reinsurance will apply to the PDIC Aus portfolio, limiting the volatility being added as a result of liabilities transferred under the scheme.

1. In relation to the financial security of Hollard policyholders, the actuary said at section 2.5.2 of the Finity Report (as written):

**2.5.2 Hollard Policyholders**

The capital adequacy provided to the Hollard policyholders is reduced post-scheme. This reflects that the liabilities of PDIC Aus but no capital are being transferred. Furthermore the PDIC Aus profitability has historically been poor, which has the potential to impact on future capital adequacy levels.

However in my opinion the financial security for the Hollard policyholders will not be materially lower post-scheme for the following reasons:

* The liabilities being transferred are small in the context of Hollard’s size.
* The performance of the PDIC Aus portfolio has already improved relative to the 2014-2016 period, reflecting both claims management and pricing initiatives that have recently been undertaken and further improvement is likely.
* The terms of the agency agreement’s, which caps commission levels if the experience is adverse, and Hollard involvement in the business mean that the risk of the PDIC Aus portfolio making underwriting losses for Hollard is reduced.
* The PDIC Aus portfolio is small relative to the Hollard business. Furthermore as Hollard’s reinsurance is applied to the PDIC Aus portfolio, the volatility is reduced.
* The support of Hollard’s parent continues to be available, if needed.

1. The November submissions at [18]-[28] are a useful summary of the changes in Hollard’s capital adequacy multiple as described by the actuary in the Finity Report, the Supplementary Report and the Second Supplementary Report (but see [24] below). Before setting them out, it is useful to know that, with effect from 31 August 2017, Hollard acquired **Calibre** Commercial Insurance Pty Ltd insurance agency from Munich Holdings Australasia Pty Ltd. The cost of acquisition was factored into the 30 September 2017 APRA capital position referred to below. From 1 April 2018 Hollard will underwrite Calibre’s portfolio. The November submissions relating to the actuary’s reports were (as written, emphasis added):

18. The Finity Report outlines the solvency position of the Australian branch of the applicant and Hollard before and after the scheme based on the 31 December 2016 APRA returns (Finity Report, Section 5). The Second Supplementary Report updates the actuary’s analysis based on the updated position of each entity at 30 September 2017 as set out in the APRA returns. The relevant portions of the actuary’s analysis are summarised below.

*The applicant’s Australian branch*

19. As at 31 December 2016, the applicant had net assets in Australia of $22.2m and a capital base of $20.1m. Its prescribed capital amount was $12.9m, giving it a capital adequacy multiple of 1.55 (Finity Report, p 20).

20. As at 30 September 2017, the applicant had a capital base of $20.1m. Its prescribed capital amount was the APRA minimum of $5m, giving it a capital adequacy multiple of 4.02. The decreased prescribed capital amount is attributable to the fact that the portfolio has been 100% reinsured by Hollard for all premiums earned since 31 March 2017 (Second Supplementary Report, p 8).

*Hollard*

21. As at 31 December 2016, Hollard had net assets of $190m and a capital base of $106.8m. Its prescribed capital amount was $65.9m, giving it a capital adequacy multiple of 1.62 (Finity Report, p 20).

22. As at 30 September 2017, Hollard had a capital base of $108.6m, a prescribed capital amount of $73.9m, and a capital adequacy multiple of 1.47 (Second Supplementary Report p 6).

*Actuarial opinion on the impact of the transfer*

23. Assuming the proposed transfer had occurred on 31 December 2016, the post-transfer capital adequacy multiple for Hollard was calculated to be 1.63 (Finity Report, p 20). Assuming the proposed transfer had occurred on 30 September 2017, the post-transfer capital adequacy multiple for Hollard is calculated to be 1.46 (Second Supplementary Report, p 7).

24. The capital adequacy multiple of 1.46 is within Hollard’s target range for operating capital, albeit it is at the lower end of that range, whereas 1.63 was at the upper end of the range (Second Supplementary Report, p 7).

25. The actuary draws attention to the impact of Hollard’s recent acquisition of the Calibre portfolio, which it will underwrite from 1 April 2018. Without any capital injection, the acquisition of that portfolio would bring Hollard’s capital adequacy multiple down to 1.34 by December 2018. However, Hollard plans to inject $40m of capital to fund the increased capital requirements resulting from the acquisition. This would increase the capital adequacy multiple to 1.74 by December 2018 (Second Supplementary Report p 8). In the event that the capital injection were delayed beyond 31 December 2017 or were not to occur, Hollard has options to reduce capital requirements (such as reinsurance and reducing growth strategies), which could have the same impact on Hollard’s capital ratio as the capital injection (Second Supplementary Report p 6).

26. In the Finity Report, the actuary formed the view that the financial security for policyholders of the applicant’s Australian branch will not be adversely affected to a material extent following the scheme (Finity Report p 7). **The actuary adheres to this view in the Second Supplementary Report, notwithstanding the fall in capital adequacy multiple from 1.63 to 1.46 (but noting this is expected to increase as the Calibre business is written and an injection of capital is made**). His reasons for forming this view are:

a. as a result of the short tailed nature of the applicant’s Australian business, the period for which transfer in policyholders are exposed to an extra risk is short (noting that they have the option at renewal to transfer to other insurers);

b. the capital adequacy multiple of 1.46 reflects a buffer of $34 million over the prescribed capital amount, which is significant;

c. Certain of Hollard’s assets which are inadmissible for APRA purposes can be seen as having some value - in effect, the capital adequacy is better than 1.46;

d. Hollard is supported by a parent company and has access to further capital. The group has demonstrated a preparedness to make capital injections where needed in the past;

e. the possibility of Hollard not being able to meet its obligations to policyholders of the applicant’s Australian branch is remote, given the buffer and noting that the prescribed capital amount represents a substantial amount of capital in its own right.

(Second Supplementary Report p 10).

27. The actuary also considers that financial security for Hollard policyholders will not be materially lower as a result of the scheme. This is notwithstanding that the capital adequacy provided to Hollard policyholders is reduced post-scheme (because the liabilities of the applicant’s Australian branch but no capital being transferred). The actuary’s reasons for this view are as follows:

a. the liabilities being transferred are small in the context of Hollard’s size (around $30m, representing about 5% of Hollard premium levels);

b. the performance of the applicant’s Australian branch has already improved relative to the 2014-2016 period, reflecting both claims management and pricing initiatives and further improvement is likely;

c. the terms of an agency agreement, which caps commission levels if the experience is adverse, and Hollard’s involvement in the business, means that the risk of the portfolio making underwriting losses is reduced;

d. the portfolio is small relative to the Hollard business and, as Hollard’s reinsurance is applied, the volatility is reduced;

e. the support of Hollard’s parent continues to be available if needed.

(Finity Report pp 6 and 7-8).

28. The actuary also points out that the applicant’s Australian business has been loss-making (with an average annual loss of $9m over three years). He does not consider this is likely to materially impact on the level of Hollard’s profits for the following reasons:

a. the losses are partly driven by the high expense ratio, averaging over 50% of the premium. Under the terms of the new Hollard agency agreement, Hollard’s expenses for the portfolio appear likely to be less than 25%;

b. the loss ratio has been well above market levels. With changes that are being made to claims management and pricing (referred to below), performance can be expected to improve.

(Finity Report p 22).

1. As noted above in paragraph [6(9)], the actuary’s view as expressed in the Second Supplementary Report was qualified: his opinion could change if the capital injection was not made and his opinion was based on the assumption that it would be made by December 2017. This qualification was not addressed expressly in the November submissions (compare the bolded words in paragraph [26] and the quoted words in paragraph [6(9)] above) nor was it expressly addressed in PDIC’s oral submissions. It should have been, having regard to the nature of the application and the fact that the actuary considered the matters addressed in paragraph [26] of the November submissions but nonetheless chose to say that his opinion could change if the capital injection was not made.
2. Counsel for Hollard raised with the Court the fact that on 1 November 2017, APRA had advised Hollard that it would require eight weeks to approve a “tier 2” instrument pursuant to which the capital injection would be made. Although the need for the capital injection and the intention that it be effected by December 2017 had been known since at least 30 August 2017, correspondence with APRA reveals that at best, the application for APRA’s approval would be made on the same day as the hearing and in any event by 17 November 2017. The expectation is that the capital injection will be able to be made by 31 January 2018.
3. Ms Neumueller advised the Court that APRA was not concerned at the one month delay in the capital injection being made. In light of APRA’s attitude and the indication that the proposed “tier 2” instrument would be provided to APRA proximately to the hearing, the reaffirmation of Hollard’s intentions in the 7 November 2017 investment intention letter and the advice that HIBV has liquid assets far in excess of the $40 million required to make the capital injection, the Court was satisfied that this issue should not prevent the orders sought by PDIC being made.

### Delay in migration of PDIC’s portfolio to the Softsure platform

1. In connection with the application for the dispensing orders, PDIC and Hollard advised the Court that it was intended that PDIA migrate the existing policy portfolio from PDIC’s software onto a new software system (**Softsure**) at the time the scheme was confirmed. However, due to the requirement for more extensive testing of the Softsure system, it was proposed that PDIA continue to use the PDIC system (which it was entitled to do) until PDIA is satisfied with the operational reliability of the new system. As there is no impediment to PDIA continuing to use the PDIC system, this issue raised no concerns.

# Conclusion

1. In all of the circumstances, the Court was satisfied that it was appropriate to make the orders sought by PDIC.

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| I certify that the preceding twenty-eight (28) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Farrell. |

Associate:

Dated: 15 January 2018